Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Annual Assessment of the Status of	)	MB Docket No. 03-172
Competition in the Market for the	)	
Delivery of Video Programming	)	
	)	

COMMENTS OF A&E AND COURT TV

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EXECUTIVE SUMMARY

There have been significant positive developments for multichannel video consumers since the FCC first began compiling data for its video competition reports. These include dramatic increases in the number of nationally delivered programming networks, decreases in vertical integration of programming services, and viewers increasingly embracing multichannel programming sources as an alternative to broadcast television. Throughout this period, the principal threats to the launch and development of new multichannel programming services have been regulatory ones, such as mandatory carriage rules and rate regulation. In each such case, the FCC eventually adjusted its rules to reduce the adverse affects that they have on programming.

In the context of rate regulation, the FCC adopted a series of remedial corrective measures to limit the significant adverse effects those rules had on the development and launch of new programming services. These measures include "going-forward" rules to provide greater economic incentives for cable operators to add channels, "new product tiers" designed to provide additional incentives for operators to provide new services, and "social contracts" which often created "migrated product tiers" as another mechanism to expand the available programming choices.

The eventual lapse of the FCC's rate regulations has prompted some groups to advocate restoring rate regulations, including proposals to require individual services to be offered à la carte. However, an à la carte pricing requirement would not lead to improved consumer welfare but would in fact result in reduced choices and higher prices for consumers. The decision to offer programming in service tiers is an editorial choice which provides the most cost-effective and beneficial manner of program delivery, ensuring lower costs and maximum choices to consumers. The cable industry continues to use tiering as its basic model for packaging and selling programming, for numerous economic and consumer-focused reasons.

Bundling of goods is a commonplace occurrence in many different markets, including in the sale of newspapers, with the various sections and columns of a daily newspaper are bundled into a single product. Similar economies are realized by offering channels in service tiers, the advantages of which include lowering transaction costs, enhancing the value of cable service for consumers, providing synergies for operators and networks associated with selling advertising and promoting services, and enabling the launch of new and unique programming services. The validity and value of using bundling for selling video programming is confirmed by the fact that it is used by virtually every entity which currently provides multichannel video or audio programming. Moreover, for new and niche programmers, obtaining carriage of a video program service in a tier with other more established programming services can mean the difference between survival and failure. Over the years, the marketplace for cable programming has thrived, due in significant part to the bundled manner in which cable operators and other multichannel video providers offer these services.

Furthermore, regulations that guarantee carriage rights or otherwise favor certain programmers necessarily create competitive imbalances in the market for video programming. As the Supreme Court observed in *Turner Broad. Sys., Inc. v. FCC*, under any must carry regime, "[b]roadcasters, which transmit over the airwaves, are favored, while cable programmers, which do not, are disfavored." The FCC recognized this imbalance when it declined to grant broadcasters dual carriage rights for both digital and analog transmissions.

Requiring broadcasters to provide hard data on their actual efforts to offer multicast programming is an essential prerequisite to the must carry rules, since affording broadcasters regulatory preference necessarily distorts the market for video programming by limiting the number of channels available for use by cable systems or cable programmers and requiring carriage decisions to be made on an unfair basis. Broadcasters whose signals are entitled to must carry status do not have to incur comparable costs of marketing their programming to prospective viewers and cable operators nor must they provide programming that is sufficiently valued in the marketplace to ensure continued delivery via cable. Although channel capacity is relevant to these issues, it is not the most important factor since the FCC here is seeking to measure the effect of its policies on video competition. Moreover, broadcasters have the benefit of must carry mandates and retransmission consent rights in addition to a slew of other regulatory and statutory benefits that broadcasters already enjoy.

The statutory and regulatory favoritism bestowed upon broadcasters by granting them must carry entitlements and retransmission consent rights disproportionately affects non-favored programmers. To the extent the government seeks to make better decisions about how to ensure a fair and properly functioning market for video programming, it must critically examine the manner in which it confers regulatory advantages upon some market participants, as is the case with must carry mandates.

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COMMENTS OF A&E AND COURT TV

A&E Television Networks, Inc. and the Courtroom Television Network LLC (collectively "A&E and Court TV") hereby respond to the Commission's Notice of Inquiry soliciting data and information for the FCC's tenth annual report on the status of competition in the market for the delivery of video programming ("*Video Competition Report*").[1]

I. BACKGROUND

Because this video competition report will be the tenth since Congress required the Commission to compile annual reports pursuant to Section 628(g) of the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Act"), the FCC has described this report as a "landmark" that will take "a broader view of the video marketplace." It will examine changes over the past year and "in the period since the first report in 1994." *NOI*, 18 FCC Rcd. at 16042. It seeks to compile not just "data and analyses on trends in the market" but also "comments on the factors that have facilitated or impeded changes in the competitive environment over these time periods." *Id*. at ¶ 2.

Although this proceeding is not a traditional rulemaking in that the Commission is not seeking comment on a particular new rule or policy, it is imperative to address the ways in

[1] *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 03-185, 18 FCC Rcd. 16042 (2003) ("*NOI*").

which past and proposed regulations have affected, and may in the future affect, the market for video programming. Indeed, data compiled in the annual video competition reports often have been cited in the Commission's regulatory decisions.[2] More directly, the *NOI* asks whether the FCC should promulgate additional rules "to promote diversity of information sources" pursuant to Section 612(g) of the Act, the extent to which channel capacity is devoted to mandatory broadcast carriage under Sections 614 and 615 of the Communications Act, and whether distributors offer or plan to offer "à la carte" programming choices, among other things. *Id*. at ¶¶ 15, 29, 32. The questions raised in the *NOI* also coincide with recent demands in some quarters to drastically re-regulate the cable industry.[3]

The focus of the video competition reports on regulatory trends as well as marketplace developments highlights the precarious position of programming networks, and especially stand-alone or independent networks, in a regulated industry. Networks are seldom subjected to direct FCC regulation, *see*, *e.g*., *Motion Picture Association of America v. FCC*, 309 F.3d 796 (D.C. Cir. 2002), yet frequently have been affected adversely by regulations directed at other parts of the industry. In this connection it is important to note that Section 628 of the Act, which addresses "competition and diversity in video programming distribution" and which

[2] *NOI*, 18 FCC Rcd. at 16058 (Statement of Comm'r Copps) (data collected in response to the NOI will "serve[ ] as the factual foundation for many Commission decisions"). *See*, *e.g*., *Implementation of the Cable Television Consumer Protection and Competition Act of 1992; Cable Home Wiring,* 18 FCC Rcd 1342 (2003); *Review of the Commission's Rules and Policies Affecting the Conversion To Digital Television,* 17 FCC Rcd 15978 (2002); and *Policies and Rules for the Direct Broadcast Satellite Service,* 17 FCC Rcd 11331 (2002).

[3] *See generally* U.S. Public Interest Research Group, *The Failure of Cable Deregulation: A Blueprint for Creating a Competitive, Pro-Consumer Cable Television Marketplace* (August 2003) (advocating, among other things, empowering state public utility commissions to regulate rates for all cable services, requiring all cable programming services to be offered on an à la carte basis, and drastically lowering rates for leased access channels) ("*The Failure of Cable Deregulation*").

established the annual video competition report requirement in subsection (g), was concerned primarily with the health of the programming sector. While the section focuses on ensuring video programming accessibility by a variety of multichannel service providers, its overall purpose is to "increase the availability of satellite cable programming." 47 U.S.C. § 628(a). For that reason, it is vital for the Commission to gather information on regulatory measures that may impede the market for cable networks to the same extent it monitors marketplace trends.[4] In this regard, the annual video competition reports thus may be viewed, at least in part, as a "regulatory impact statement" on programming issues.

In the decade since the Commission first began compiling data for its video competition reports, there have been significant positive developments for multichannel video consumers. The number of nationally delivered programming networks has steadily increased more than three-fold, from less than 100 in the first video competition report to 308 in the ninth annual report.[5] During this time, the level of vertical integration of programming services, as measured by the Commission, declined from 53 percent to 30 percent. *Compare First Report*, 9 FCC Rcd. at 7522, with *Ninth Report*, 17 FCC Rcd. at 26959. By any measure the variety of programming services and options available to the average subscriber has been greatly enhanced,

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[4] *Cf.* Section 202(h) of the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (requiring biennial regulatory review).

[5] *See generally Implementation of Section 19 of the 1992 Cable Act (Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming)*, 9 FCC Rcd. 7442 (1994) ("*First Report*"); 11 FCC Rcd. 2060 (1995) ("*Second Report*"); 12 FCC Rcd. 4358 (1997) ("*Third Report*"); 13 FCC Rcd. 1034 (1998) ("*Fourth Report*"); 13 FCC Rcd. 24,284 (1999) ("*Fifth Report*"); 15 FCC Rcd. 978 (2000) ("*Sixth Report*"); 16 FCC Rcd. 6005 (2001) ("*Seventh Report*"); 17 FCC Rcd. 1244 (2002) ("*Eighth Report*"); and 17 FCC Rcd. 26,901 (2002) ("*Ninth Report*").

both in quality and quantity.[6] And, as might be expected, viewers increasingly have embraced multichannel programming sources as an alternative to broadcast television.[7] The number of households subscribing to cable television increased from 57.4 million to 68.8 million during the period covered by the nine previous reports, while the number of subscribers to DBS rose from 40,000 to 18.2 million.[8] The total number of subscribers to all multichannel video services reached 89.9 million households by mid-2002. *Ninth Report*, 17 FCC Rcd. at 26953.

Throughout this period of positive growth, the principal threats to the launch and development of new multichannel programming services were regulatory, as the Commission itself came to recognize. Mandatory carriage rules established governmental preferences for broadcast programming over satellite-delivered services and rate regulations stifled the ability of operators to add new services. In many cases, plans to launch new programming networks were delayed, and in some instances abandoned altogether.[9] The Commission took corrective action

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[6] *See* Eli M. Noam, *Public-Interest Programming by American Commercial Television*, *in* PUBLIC TELEVISION IN AMERICA 145-176 (Eli M. Noam & Jens Waltermann eds., 1998) (the number of channels found to provide "primarily public-interest programming" was considered to be quite large, representing almost half of the available cable channels).

[7] In the *First Report* the Commission found that the four broadcast networks (ABC, CBS, NBC and Fox) had 72 percent of the prime time audience during the 1993-94 season, while in the Ninth Report, all broadcast stations, including the top *seven* broadcast networks, had a combined prime time audience share of 58.9 percent (2001-02 season). *See Ninth Report*, 17 FCC Rcd. at 26941. The prime time audience share for the top four broadcast networks was 45 percent in 2002.

[8] *Compare First Report*, 9 FCC Rcd. at 65, with *Ninth Report*, 17 FCC Rcd. at 26929-30. This represents more than 20 percent of the multichannel video market. *Id*. at 26903.

[9] *See*, *e.g.*, Thomas W. Hazlett, *Digitizing "Must-Carry" Under Turner Broadcasting v. FCC (1997)*, 8 SUP. CT. ECON REV. 141, 173-174 (2000) ("C-Span or C-Span2 was curtailed in nearly ten million households pursuant to the 1992 Cable Act, of which nearly five million were specifically due to must-carry"). *See also id*. at 187 ("As an economic matter, intensifying cable carriage congestion for upstart cable networks inhibits network formation, since new ventures are particularly vulnerable to delays in gaining nationwide audiences.").

in some cases, but anticipating such adverse effects and gathering the information necessary to help avoid such situations which undermine the stated goal of increased program diversity is a far better policy. Accordingly, the Commission's tenth *Video Competition Report* provides an important opportunity to do just that. It also provides an opportunity to examine issues that may become more significant in the coming decade.

II. RATE REGULATIONS IMPLICATE ISSUES OF VIDEO COMPETITION

A. The Commission Historically Has Adjusted its Rules to Reduce Adverse Effects on Programming

Rate regulations adopted pursuant to the Cable Act of 1992 had significant adverse effects on the development and launch of new programming services. In response to these adverse effects, the Commission implemented a series of remedial corrective measures.[10] Under the FCC's initial rate regulations, the only vehicle for operators to recover costs of adding new channels was an unwieldy cost-of-service methodology. The rules had created an artificial bottleneck that was stalling new launches and stifling existing services. When the Commission was made aware of this problem, it developed "going-forward" rules to provide greater economic incentives for cable operators to add channels. The FCC revised its rules "[b]ecause appropriate incentives for adding new channels serves the statutory goal of 'promot[ing] the availability to the public of a diversity of views and information.'"[11]

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[10] Thomas W. Hazlett, *Prices and Outputs Under Cable TV Reregulation*, 12 J. OF REGULATORY ECON. 173 (1997) (The growth rate of basic cable television subscribership fell sharply during the period of rate reductions. Only after rate controls were relaxed in response to concerns about their impact on programming networks did industry output measures return to the pre-regulation growth trends).

[11] *Rate Regulation, Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking*, 10 FCC Rcd. 1226, 1231 (1995). The revised "going-forward" rules were designed to "benefit consumers by assuring that operators will have incentives to add new services." *Id.* at 1248.

As part of these changes, the Commission created "new product tiers" ("NPTs") which consisted of new services (which could be offered in combination with other services already carried on other tiers). NPTs were designed to "provide additional incentives for operators to provide new services to consumers because operators will be permitted to price these tiers as they choose."[12] When the FCC created NPTs, it acknowledged the shortage of channel capacity for new services and ruled that the public interest would be served by policies designed to "create additional capacity for new services" on cable systems. It also sought to help programmers "establish an audience for their new channels."[13] In addition to modifying the "going forward" rules to coincide with the goal of promoting diversity, the FCC also issued a number of declaratory rulings and waivers to facilitate launches of new programming services. For example, the FCC waived the rules to permit cable operators to pass through immediately the launch costs for one new service where the rules would have otherwise required a waiting period before those costs could have been recovered by cable operators.[14]

In another effort to relieve disincentives to add new programming networks to cable systems, the FCC developed the concept of flexible "social contracts" as an exercise in regulatory forbearance. The Commission entered into social contracts with a number of cable operators for the purpose of resolving rate complaints, many of which provided for the creation

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[12] *Id.* at 1234.

[13] *Id.* at 1235-36. In addition, small system operators were permitted to use a streamlined cost-of-service methodology to justify rate increases based on channel additions. *Id.* at 1257-59.

[14] *Letter to Robert Corn-Revere from Alexandra M. Wilson* (released April 19, 1994). In another ruling, the FCC determined that marketing expenses for which cable operators were reimbursed by a programmer did not have to be offset against increases in programming costs for calculation of external cost pass-throughs. *Letter to Frederick Kuperberg from Kathleen M. H. Wallman,* 9 FCC Rcd. 7762 (CSB 1994). The FCC also relaxed notice requirements to facilitate new launches. *See, e.g.*, *Letter to Michael Ruger from Meredith J. Jones*, 10 FCC Rcd. 3207 (CSB 1995).

of migrated product tiers ("MPTs").[15] The FCC created NPTs and MPTs "to expand the programming choices available for subscribers."[16] The Commission concluded that it could conduct its proceedings "in such a manner as will best conduce to the proper dispatch of business and to the ends of justice."[17] It found that its goals to "simplify" regulation and "afford adequate protection for subscribers [and others]" were served by a flexible approach, rather than by strict application of regulation.[18]

The Commission's rate regulations eventually were allowed to lapse. *In the Matter of Implementation of Cable Act Reform Provisions of the Telecommunications Act of 1996*, 14 FCC Rcd. 5296 (1999). This has prompted some groups to advocate restoring rate regulations, including proposals to require individual services to be offered à la carte. Such proposals generally assume – without analysis or evidence – that such a requirement would enable consumers to control cable television rates. *See*, *e.g.*, *The Failure of Cable Deregulation*, *supra* note 3 at 57. However, as explained below, such assumptions are unwarranted and the regulatory proposals on which they are based would undermine the Commission's goal to promote programming availability.

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15 *See, e.g., Cox Communications, Inc. Social Contract*, 11 FCC Rcd. 1972, 1985 (1996).

16 *Id.* Migrated product tiers permit operators more flexibility than "new product tiers" because programming services may be moved from a regulated tier to a migrated product tier. New product tiers, on the other hand, consist only of new services and services carried duplicatively from other tiers.

17 *Comcast Cable Communications, Inc., Final Resolution of Cable Programming Service Rate Complaints, Order*, 11 FCC Rcd. 4029 (1996), citing Communications Act § 4(j), 47 U.S.C. § 154(j).

18 *Id.* at 4033.

B. Requiring Cable Operators to Provide Channels À la Carte Would Undermine the Market for Programming Networks

The concept of requiring cable operators to make programming available on an à la carte basis has been raised from time to time, although neither Congress nor the Commission has come close to imposing such a rule. Indeed, the 1992 Cable Act operates on the assumption that cable operators must have discretion to structure their various tiers of programming (other than the basic tier, which must include local broadcast signals and access channels).[19] Nevertheless, in each of its last five annual video competition reports, the Commission has requested comment on how video program distributors package and market their programming and the extent to which distributors offer programming on an à la carte basis.[20] This year, in its stated effort to take a broader view of the video marketplace and possibly establish the basis for future regulation, the Commission has again asked for comment on this issue. *See NOI*, FCC 03-185 at ¶ 15. However, an à la carte pricing requirement would not lead to improved consumer welfare. To the contrary, requiring operators to offer cable programming on an à la carte basis would result in reduced choices and higher prices for consumers.

Program bundling is critical both to cable programmers and the cable television industry. The decision to offer programming in service tiers is an editorial choice,[21] and it

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[19] 47 U.S.C. § 543(b). *See Rate Regulation Report & Order*, 8 FCC Rcd. 5631, ¶ 440 (1993) (rate regulations were not intended to reduce cable operators' discretion to decide which services to include in various tiers of service); *Time Warner Cable v. Doyle*, 66 F.3d 867 (7th Cir. 1995).

[20] *See Fifth Report,* 13 FCC Rcd. at 24387-89*; Sixth Report,* 15 FCC Rcd. at 1064-65; *Seventh Report,* 16 FCC Rcd. at 6085; *Eighth Report,* 17 FCC Rcd. at 1316-17; *and Ninth Report,* 17 FCC Rcd. at 26964-65.

[21] *E.g.*, *Hurley v. Irish-American Gay, Lesbian and Bisexual Group of Boston*, 515 U.S. 557, 570 (1995) (the selection of programming by cable operators in an editorial function protected by the First Amendment).

provides the most cost-effective and beneficial manner of program delivery, ensuring lower costs and maximum choices to consumers. Cable television programming has generally been offered to customers in packages or tiers since the early days of the cable television industry. *See Fifth Report,* 13 FCC Rcd. at 24387. Even before the advent of satellite-delivered programming, cable operators packaged local television channels together and sold them to customers as a "community antenna" service. When cable systems began to offer programming services they received by satellite, the operators included these programs in the same level of service with the retransmitted broadcast stations or sold them on a "tier," with premium channels and local sports programming being offered separately on a per-channel or per-program basis.

The cable industry continues to use this basic model for packaging and selling its programming, for numerous economic and consumer-focused reasons which remain as valid today as they were when the cable industry began. According to an economic study filed with the Commission in connection with its *Fifth Report*,[22] which remains the most authoritative analysis of channel tiering which has been submitted to the Commission in its video competition inquiries, bundling of goods is a commonplace occurrence in many different markets. Potentially distinct products are often bundled in order to lower transaction costs, benefit from scale and scope economies, and enhance the attractiveness or convenience of the product to consumers. *See* Economists Study at 1. In the sale of newspapers, for example, the various sections and columns of a daily newspaper are bundled into a single product, even though not everyone who purchases a newspaper reads every part of it. But a newspaper is sold as a bundled product because: (1) the economies in having all sections delivered at once rather than

[22] "How Bundling Cable Networks Benefits Consumers," Economists, Incorporated, July 23, 1998 ("Economists Study"), filed with Comments of ABC, Inc., CS Docket No. 98-102, July 31, 1998.

having separate distribution mechanisms for each section; (2) the value to subscribers of having the option to look at all of the sections, even if they do not read all sections every day; and (3) bundling makes advertising more valuable and efficient because advertisers prefer paying a single price to reach all of the newspaper's readers with a single advertisement, rather than placing an advertiser's separate ads in each newspaper section. *Id.* at 1-2. For much the same reason, encyclopedias are sold in sets and not as individual volumes.

Similar economies are realized by offering channels in service tiers. The advantages of bundling cable network offerings include lowering transaction costs and enhancing the value of cable service for consumers, providing synergies for operators and networks associated with selling advertising and promoting services, and enabling the launch of new and unique programming services. *Id*. at 2-5. Basic economic analysis confirms that the cost of service will necessarily increase if individual channels are sold in separate units. *See generally* Bruce Owen and Stephen Wildman, VIDEO ECONOMICS 219-20 (1992) ("Owen & Wildman"). The validity and value of this approach for selling video programming is confirmed by the fact that bundling is used by virtually every entity which currently provides multichannel video programming. Program bundles similar to those offered by cable operators are also offered by DBS providers, OVS operators, C-Band satellite providers, and wireless cable providers.[23] It also is noteworthy that even the two national DARS providers use a tiering approach to sell their multichannel audio services.

For new and niche programmers, obtaining carriage of a video program service in a tier with other more established programming services can mean the difference between

[23] The fact that every multichannel video provider packages and sells its services in essentially the same way negates any argument that cable sells programming through bundles

survival and failure. A new program service's placement on a cable service tier, especially in proximity to the channel numbers of the most widely watched programming, will help ensure that the service gets introduced to an audience, in much the same way as broadcast networks choose to place new programs in time slots adjacent to established programs. As the Economists Study explains, "[i]t is through that association that new services have the greatest opportunity to be sampled and hence to find an audience." Economists Study at 4. Stated another way, "[b]y aggregating the demands of viewers who differ in their willingness-to-pay for different services, bundling makes it possible to supply program services that could not be supported on a stand-alone basis." Owen & Wildman at 134. Indeed, the failure rate among cable services that have been offered on an à la carte basis, and the trend of program services to migrate from à la carte to tiers (*e.g.* Bravo and Disney), demonstrates the risks inherent in cable carriage without the benefit of bundling.[24]

The Commission has acknowledged the application of these basic economic principles in the multichannel environment. In adopting rules for local broadcast carriage on DBS systems, the Commission prohibited DBS providers from carrying some local stations in a bundled package and others on an à la carte basis. Based on the potential unfairness to a station

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based on some perceived monopoly or anti-competitive power. To the contrary, bundling is used throughout the multichannel video industry because it makes economic sense to do so.

[24] Economists Study at 6. The fact that programming serving discrete markets benefit from carriage in packages with other established services is undeniable. For example, on the Montgomery County, Maryland cable system, two niche sports programming services, The Outdoor Life Network and The Golf Channel, are offered on the analog expanded basic service as part of a sports block on channels 42 through 46 which includes the more widely-viewed services of ESPN, ESPN2, and Comcast SportsNet. Absent carriage on a tier with better established sports services, more specialized programming such as these two services might be unable to survive. Even when new services aren't located in close proximity to channels serving a similar demographic audience, a consumer's channel surfing on a tier often introduces him or her to new networks that can become favorites in the future.

that was excluded from the package, the Commission found that "[a]llowing satellite carriers to offer some stations as a package and others on an à la carte basis could operate as a deterrent to the purchase of certain local stations without furthering consumer choice."[25]

In sum, the marketplace for cable programming has thrived, due in significant part to the bundled manner in which cable operators and other multichannel video providers offer these services. This economic model has enabled programmers to invest in original programming, which in turn has attracted a growing number of viewers to cable and other multichannel media.[26] No evidence exists of any dysfunctional marketplace which calls for the Commission's involvement. Rather, cable operators carry programming in a manner that is responsive to their customers' needs and interests and in a manner that has led to the creation of hundreds of diverse programming services. The fact that cable operators offer most of their programming in packages is due to marketplace necessities and customer demands. Encouraging or mandating à la carte channel carriage is a solution in search of a problem.

III. MANDATORY CARRIAGE OBLIGATIONS IMPLICATE ISSUES OF VIDEO COMPETITION

Regulations that guarantee carriage rights or otherwise favor certain programmers necessarily create competitive imbalances in the market for video programming. The Commission recognized this issue when it established market-based rates for leased access channels pursuant to the 1992 Cable Act, citing its desire to promote the "growth and continued

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[25] *Implementation of the Satellite Home Viewer Improvement Act of 1999: Broadcast Signal Carriage Issues,* 16 FCC Rcd. 16544, 16568 (2001), *aff'd sub nom Satellite Broadcasting and Communications Association v. FCC*, 275 F.3d 337 (4th Cir, 2001).

[26] According to a study released by the National Cable and Telecommunications Association ("NCTA"), between 19997 and 2002, basic cable program networks increased their investment for original programming and program acquisition by 115 percent, from $4.3 billion to $9.2 billion, which has led to substantial increases in the viewership of cable programming. "Cable Pricing, Value, and Costs," NCTA White Paper, p. 5 (May, 2003).

development of cable systems" and its goal to avoid "requiring the operator to bump existing programming."[27] The same principle applies to mandatory carriage of broadcast signals, since under any must carry regime, "[b]roadcasters, which transmit over the airwaves, are favored, while cable programmers, which do not, are disfavored." *Turner Broad. Sys., Inc. v.* FCC, 512 U.S. 622, 645 (1994). It is indisputable that "compulsory carriage … displace[s] cable program providers," *Turner Broad. Sys., Inc. v. FCC*, 520 U.S. 180, 226 (1997) ("*Turner II*") (Breyer, J., concurring in part), by limiting their opportunities for carriage in a concrete, measurable way.[28] The leverage created by retransmission consent rights has a similar effect that benefits some programmers to the detriment of others.[29]

The Commission recognized these effects when it declined to grant broadcasters dual carriage rights for both digital and analog transmissions. Specifically, the Commission determined that requiring cable operators to carry both a broadcaster's analog signal and its

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[27] *Second Report and Order and Second Order on Reconsideration of the First Report and Order*, 12 FCC Rcd. 5267, 5281 (1997) ("*Second Order on Reconsideration*"). Although it initially proposed a cost -based approach to establish maximum permitted leased access rates, *Order on Reconsideration of the First Report and Order and Further Notice of Proposed Rulemaking*, 11 FCC Rcd. 16934, 16953 (1996), the Commission ultimately based such rates on the average implicit fee for similar channels. *Second Order on Reconsideration*, 12 FCC Rcd. at 5282.

[28] For every broadcast offering cable operators are required to carry – regardless of whether viewers want them or would prefer other programming – another programming source loses a potential programming opportunity. *See Turner II*, 520 U.S. at 214 (discussing "limited channels remaining" to cable programmers).

[29] Retransmission consent rights enable program providers who already wield sufficient market power to secure carriage of their broadcast signal to demand carriage of unrelated, non-broadcast programming. Under such arrangements, the unrelated programming garners carriage not by fostering viewer demand or otherwise proving its worth in head-to-head competition in the market, but rather simply by being under common control with a broadcast offering entitled to mandatory carriage. This favors the largest broadcasters, who remain among the most powerful market participants. Meanwhile, other programmers must compete in the market to build demand for their offerings by producing compelling programming that viewers desire.

digital signal during the DTV transition would impose too great a burden on cable operators' First Amendment rights to survive constitutional review. *Carriage of Digital Television Broadcast Signals*, 16 FCC Rcd. 2598, 2605 (2001) ("*Digital Must Carry Order*"). It also determined that, as applied to digital broadcast signals, the requirement that cable operators must carry a broadcaster's "primary video" signal[30] means one programming stream and its program-related content, even if the broadcaster uses its digital allotment to multicast several program offerings. *Id*. at 2622 ("'primary video' means a single programming stream and other program-related content").

At the same time, however, the Commission left the door open to the possibility that it may yet grant broadcasters additional must carry rights. It deemed its decision that a dual carriage requirement would violate the First Amendment as merely "tentative," and it solicited further comment on a range of underlying issues, including channel capacity, and what broadcast material is "program related" for purposes of what must be carried as part of a broadcaster's "primary video."[31] This has led to further demands from broadcasters for multicast carriage rights, but what has been missing from the dialogue is evidence of the actual need for such carriage. Accordingly, the current *NOI* asks, among other things, "[h]ow many broadcasters are using their DTV channels to offer multicast DTV and how many cable operators are carrying multicast DTV or would be willing to do so if and when broadcasters transmit multiple streams?" The Commission also requested comment on "the impact these new services and

[30] 47 U.S.C. §§ 534(b)(3), 535(g)(1).

[31] *Digital Must Carry Order*, 16 FCC Rcd. at 2647-49, 2651-54. Broadcasters have taken this opportunity to demand both dual carriage and full multicast carriage for all their program streams, regardless of their relation to one another, and the Commission has yet to definitively resolve these questions, although the matter has been pending for over two years.

technologies will likely have on traditional video programming distribution and viewing." *NOI*, FCC 03-185 at ¶ 20.

Requiring broadcasters to provide hard data on their actual efforts to offer multicast programming is an essential prerequisite to the contemplation of must carry rules, since granting them a regulatory preference would necessarily distort the market for video programming. This distortion would manifest itself not just in the number of channels that remain available for use by cable systems or cable programmers – though that is surely part of the equation – but also in the way that the statutory and regulatory regimes cause carriage decisions to be made on an unfair basis. Broadcasters whose signals are entitled to must carry status do not have to incur comparable costs of marketing their programming to prospective viewers and cable operators. Nor must they concern themselves with maintaining programming that is sufficiently valued in the marketplace to ensure continued delivery via cable. Although channel capacity is relevant to these issues, it is not the most important factor since the Commission here is seeking to measure the effect of its policies on video competition. Granting a regulatory advantage to one class of programmers necessarily has an adverse effect on the disfavored class.[32]

Unlike broadcasters, cable programmers must continually prove their value through programming investments and marketing, measured against daily ratings and other cable

[32] The fact that larger cable systems have upgraded and expanded capacity is not a panacea since the range of services being provided has also grown. As of the last *Video Competition Report*, the FCC listed more than 300 national video programming services, nearly 100 regional programming services, and several dozen more program services prepared to launch. *See Ninth Report*, 17 FCC Rcd. at Tables C-1, C-2, C-3, C-4. In addition, a host of new services compete for bandwidth on cable systems, including high-speed Internet access, IP telephony, pay-per-view services, interactive television and digital audio, to name a few. The channel capacity of even the largest cable systems cannot begin to keep up with this range of new and existing services.

channels competing for valuable channel positions and distribution. In addition, must carry broadcasters are never required to pay for carriage, and in fact are statutorily barred from doing so, *see* 47 U.S.C. § 614(b)(10), while many cable networks have no choice but to respond to marketplace realities by paying per-subscriber marketing support and launch fees to obtain carriage.

The great ironies of the competitive imbalance fostered by must carry mandates and retransmission consent rights is that they have been conferred on top of a slew of other regulatory and statutory benefits that broadcasters already enjoy, and that in fact may not even be necessary. To date, broadcasters repeatedly have enjoyed significant regulatory advantages, including billions of dollars worth of free spectrum – first analog and then digital – with no firm deadline for returning one of the allotments after the digital transition; preferential channel placement rights that accompany mandatory carriage guarantees; and the ability to flexibly use additional broadcast spectrum, conveyed at no charge to facilitate the digital transition, for innovative, for-profit ventures. At the same time, the Commission's internal analyses suggest that broadcasters are more than able to compete if forced to do so.[33] As one Commissioner recently put it, broadcasters may continue to claim that "free over-the-air television is threatened" but "the rumors of its demise … are greatly exaggerated."[34]

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[33] *See also* Jonathan Levy, et al., *Broadcast Television: Survivor in a Sea of Competition*, Federal Communications Commission, Office of Plans and Policy Working Paper 37, 2 (Sept. 2002) ("OPP Working Paper 37") ("technological developments such as Interactive Television hold out the possibility of preserving and even enhancing broadcast television's advertising base").

[34] *2002 Biennial Regulatory Review -- Review of the Commission's Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act 1996*, 18 FCC Rcd. 13620 (2003) (Comm'r Adelstein dissenting).

Indeed, the Commission's former Office of Plans & Policy ("OPP") recently reported that "[b]roadcasting has survived a substantial increase in multichannel video programming distribution penetration" and that "[d]espite … proliferation in the number of non-broadcast programming networks, and … in the availability of non-broadcast programming, broadcasters still attract substantial revenues[.]" OPP Working Paper 37 at 1-2. It also reported that "[n]o broadcast stations have turned in their licenses and gone dark" and, in fact, "the number of full power stations has increased substantially over the last ten years." *Id*. at 18.

At the same time, the OPP acknowledged the importance and strength of non-broadcast programming in the marketplace. It found that the "larger quantity of desirable programming on cable almost surely … play[ed] a role" in helping to expand total television viewing over the last ten years. *Id*. at 19. The OPP also noted that, "based on revealed subscriber willingness to pay, … cable and DBS subscribers value those services highly." *Id*. at 8. In other words, cable programmers have established themselves in the marketplace even though they were not accorded any of the government subsidies lavished on broadcasters.

Both the continuing competitive advantage that must carry generally confers on broadcasters and the lack of finality in the Commission's digital must carry proceeding constitute "remaining or impending statutory or regulatory barriers to new entrants in the video market" as well as "economic [and] legal … factors that affect [the] ability to offer … service" that more closely reflects consumer demands. *NOI*, FCC 03-185 at ¶¶ 8, 15. The statutory and regulatory favoritism bestowed upon broadcasters by granting them must carry entitlements and retransmission consent rights disproportionately affects non-favored programmers. To the extent the government seeks to "make better decisions" about how to ensure a fair and properly functioning market for video programming,[35] it must critically examine the manner in which it confers regulatory advantages upon some market participants, as is the case with must carry mandates. Such a critical examination requires, at a minimum, that the Commission compile hard data on the type of programming (*e.g.*, multicast broadcasting) it seeks to favor.

CONCLUSION

The Commission has designated this tenth video competition report as a landmark in which it plans to take a broader view of the video marketplace so as to better assess the factors that have facilitated or impeded changes in the competitive environment. An important step in this direction would be to view this report as a regulatory impact statement, to give serious attention to the ways in which FCC rules have affected competition in the market for video programming.

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[35] *NOI*, 18 FCC Rcd. 16058 (Statement of Comm'r Copps).